UNITED NATIONS

A

General Assembly

Distr.
GENERAL

A/CN.9/444/Add.5
2 March 1998

ORIGINAL: ENGLISH

UNITED NATIONS COMMISSION
ON INTERNATIONAL TRADE LAW
Thirtieth session
New York, 1-12 June 1998

PRIVATELY FINANCED INFRASTRUCTURE PROJECTS

Draft chapters of a legislative guide on privately financed infrastructure projects

Report of the Secretary-General

Addendum

Chapter IV. CONCLUSION AND GENERAL TERMS OF THE PROJECT AGREEMENT

	Paragraph	Page
Legislative recommendations	-	2
Notes on legislative recommendations	1-48	4
Section		
A. General considerations	1-6	4
1. Legislative approaches	1-4	4
2. Conclusion of the project agreement	5-6	4
B. General terms of the project agreement	7-47	5
1. The project site	8-12	5
2. Easements	13-16	7
3. Exclusivity	17-21	7
4. Legal status of the concessionaire	22-34	9
5. Assignment of the concession	35-38	12
6. Security interests	39-45	13
7. Duration	46-47	15
C. Specific terms	48	15

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LEGISLATIVE RECOMMENDATIONS

Legislative approach to the project agreement

(1) It is advisable to limit the legislative provisions on the mutual rights and obligations of the host Government and the project company to those strictly necessary, such as provisions on matters for which prior legislative authorization might be needed, or that might affect the interests of third parties or that relate to essential policy matters (see paras. 2-4).

Conclusion of the project agreement

(2) It is advisable to simplify the procedures for the conclusion of the project agreement and to identify in advance the authority or authorities competent to approve and sign the project agreement on behalf of the host Government (see paras. 5-6).

The project site

(3) Where the land for the project site has to be acquired by the host Government through expropriation, it may be desirable to provide that all expropriations required for privately financed infrastructure projects be carried out pursuant to the most expeditious proceedings available under the laws of the host country (see paras. 8-12)

(4) Easements that might be needed by the project company may be provided in sector-specific legislation (see paras. 13-16).

Exclusivity

(5) It is advisable for the law to leave it for the host Government and the project company to agree on whether the host Government needs to undertake not to facilitate or support the execution of a parallel project that might generate competition to the project company (see paras. 17-21).

Legal status of the concessionaire

(6) The host Government may wish to require that project consortia establish an independent legal entity with a seat in the country. Where deemed to be in the public interest, the law may authorize the host Government to award projects to foreign companies (see paras. 26-27).

(7) It may not be advisable to set forth the legislative requirement of a fixed sum as minimum capital (see paras. 29-30).

(8) The law might require that the activities of the project company be limited to the development and operation of a particular project or projects awarded to the project company.

The law might further require that fundamental changes in the statutes and by-laws of the project company or the transfer of effective control over the project company need to be approved by the host Government (see paras. 31-34).

Assignment of the concession

(9) The project company should not have the right to assign the concession without the consent of the Government. The conditions under which an approval to the assignment of a concession prior to its expiry may be granted may include:

(a) acceptance by the new concessionaire of all obligations under the project agreement;

(b) evidence of the new concessionaire's technical and financial capability as necessary for providing the service (see paras. 35-36).

(10) The concessionaire may be authorized to award subconcessions, subject to prior approval by the host Government (see paras. 37-38).

Security interests

(11) Where the physical assets comprised in the infrastructure are not owned by the project company, it advisable for the law to clarify whether and to what extent the project company may create security interests over those assets (see paras. 40-42).

(12) It is useful for the law to enable the project company to create security over the rights arising out of the project agreement, provided that the enforcement of such security does not affect the obligations of the project company under the agreement (see paras. 43-44).

(13) It is further useful for the law to authorize the creation of security interests over the shares of the project company, subject to the approval of the host Government (see below, para. 45).

Duration

(14) Where it is found desirable to adopt legislative provisions limiting the duration of concessions to a maximum number of years, it is advisable to provide a period sufficiently long to allow the project company to repay its debts and to achieve a reasonable revenue, production or usage level (see paras. 46-47).

NOTES ON LEGISLATIVE RECOMMENDATIONS

A. General considerations

1. The "project agreement" between the Government and the project company is the central document in an infrastructure project. The project agreement defines the scope and purpose of the project, the rights and obligations of the parties; it provides details on the works to be performed by the project company and sets forth the conditions for the operation of the infrastructure or the delivery of the relevant services.

1. Legislative approaches

2. Three main approaches have been used by national legislation with regard to the content of the project agreement. The laws of some countries scarcely refer to this type of agreement, while the laws of other countries contain extensive mandatory provisions concerning the content of clauses to be included in the agreement. An intermediate approach is taken by those national laws that list a number of issues to be addressed in the project agreement without regulating in detail the content of its clauses.

3. Legislative provisions on certain essential elements of the project agreement may serve the purpose of establishing at the outset of negotiation a general framework for the allocation of rights and obligations between the parties. They may be intended to provide legislative guidance to the public authorities involved in the preparation of project agreements at different levels of Government (national, provincial or local). Such guidance may be found particularly useful by public authorities lacking experience in the negotiation of project agreements. Some countries may further consider that legislative provisions on certain elements of the project agreement may enhance the Government's negotiating position vis-à-vis the project company. Lastly, legislation may sometimes be required so as to provide the Government with the authority to agree on certain types of provisions.

4. The possible disadvantage of legislative provisions dealing in detail with the rights and obligations of the parties is that they might deprive the Government and the project company of the necessary flexibility to negotiate an agreement that takes into account the needs and particularities of a specific project. Therefore, it is advisable to limit the scope of legislative provisions concerning the project agreement to those strictly necessary, such as, for instance, provisions on matters for which prior legislative authorization might be needed or those that might affect the interests of third parties or provisions relating to essential policy matters on which variation by agreement is not admitted.

2. Conclusion of the project agreement

5. Privately financed infrastructure projects are typically carried out pursuant to written agreements between the Government and the project company. The negotiation and signature of a written agreement is often expressly required by the law. Some national laws prescribe certain

formalities for the conclusion and entry into force of the project agreement. In some countries the terms of the agreement negotiated between the awarding authority and the selected project consortium may be subject to approval by a higher authority. Sometimes the entry into force of the project agreement is subject to an act of parliament or even the adoption of special legislation.

6. With a view to expediting matters and avoiding the adverse consequences of delays in the project's timetable, in some countries the authority to bind the host Government is delegated in the relevant legislation to designated officials, so that the entry into force of the project agreement occurs upon signature or upon the completion of certain formalities, such as publication in the official gazette. In countries where such a procedure might not be feasible, or in which final approvals by another entity would still be required, it would be desirable to consider ways to avoid unnecessary delay. It is important to bear in mind that the risk of the project being frustrated by lack of approval after negotiations have been completed is not one that the project company would be ready to assume. Where approval requirements are perceived as arbitrary or cumbersome, the host Government might be requested to provide sufficient guarantees to the project company and the lenders against such risk. In some countries where those approval requirements exist, Governments have sometimes agreed in the project agreement to compensate the project company for all costs incurred in the event the final approval of a project is withheld for reasons not imputable to the project company.

B. General terms of the project agreement

7. Project agreements are typically lengthy documents that deal extensively with a wide variety of general and project-specific issues. Possible legislative implications of what in national laws appear to be core provisions are discussed in this section.

1. The project site

8. Where a new infrastructure facility is to be built on land owned by the host Government, or an existing infrastructure facility is to be modernized or rehabilitated (such as in "modernize-operate-transfer" or "rehabilitate-operate-transfer" projects), it will normally be for the host Government, as the owner of such land or facility, to make it available to the project company. The host Government may either transfer to the project company title to the land or facilities or retain title thereto, while granting the project company a right to use the land or facilities and build upon it.

9. Both in cases where the infrastructure facility will be transferred back to the host Government or will be permanently owned by the project company, it is advisable that the parties establish the condition of such land and facility at the time it is handed over to the project company. Such determination may reduce disagreements at the time the infrastructure facility is returned to the host Government. Therefore, the project agreement should provide for the inspection, measurement and demarcation of such land and existing facility prior to its being transferred or made available to the project company. Further matters which would be typically

dealt with in the project agreement include procedures for handing over the land or facilities and the submission of required documentation.

10. The situation may become more complex when the land is not already owned by the host Government and needs to be purchased from its owners. In the case of projects that originate from an unsolicited proposal from the private sector (see chapter III, "Selection of the concessionaire", paras. 87-93) or infrastructure facilities of relatively high commercial potential that are not deemed to be a national priority, the host Government might not see a compelling reason for undertaking to acquire the land and make it available to the project company. In most cases, however, the project company may not be in the best position to assume the responsibility for purchasing the land needed for the project. The project company may fear the potential delay and expense involved in negotiations with possibly a large number of individual owners and, as necessary in some parts of the world, to undertake complex searches of title deeds and review of chains of previous property transfers so as to establish the regularity of the title of individual owners. Therefore, it is typical for the host Government to assume the responsibility for providing the land required for the implementation of the project, so as to avoid unnecessary delay or increase in the project cost as a result of the acquisition of land. The host Government may purchase the required land from its owners or, if necessary, acquire it through expropriation.

11. Where expropriation procedures are required, various preparatory measures may need to be taken to ensure that construction works are not delayed. In countries where the law contemplates more than one type of expropriation proceedings, it may be desirable to provide that all expropriations required for privately financed infrastructure projects be carried out pursuant to the more expeditious of those proceedings, such as the special proceedings that in some countries apply for reasons of compelling public need (see chapter I, "General legislative considerations", paras. 36-37).

12. The right to expropriate private property is usually vested in the Government, but the laws of a number of countries also authorize public utilities or public service providers (e.g. railway companies, electricity authorities, telephone companies) to perform certain actions for the expropriation of private property required for providing or expanding their services to the public. Particularly in those countries where the award of compensation to the owners of the property expropriated is adjudicated in court proceedings, it has been found useful to delegate to the concessionaire the authority to carry out certain acts relating to the expropriation, while the host Government remained responsible for accomplishing those acts that, under the relevant legislation, are conditions precedent to the initiation of expropriation proceedings. Upon expropriation, title to the land is often vested in the host Government, although in some cases the law may authorize the host Government and the project company to agree on a different arrangement, taking into account their respective shares in the cost of expropriating the property.

2. Easements

13. Besides the acquisition of property for the construction of the facility, there might be a need for ensuring the project company's access to such property, in cases where the location of the site of the project is such that access to it requires transit on or through the property of third parties. The nature of the project may also be such that it requires the project company to enter property belonging to third parties (e.g. to place traffic signs on adjacent lands; to install poles or electric transmission lines above third parties' property; to install and maintain transforming and switching equipment; to trim trees that interfere with telephonic lines placed on abutting property). The right to use another person's property for a specific purpose or to do work on it is generally referred to in the *Guide* by the word "easement".

14. Easements usually require the consent of the owner of the property to which they pertain, unless such rights are provided by the law. Except for cases where the required easements affect only a small number of adjacent properties, it is usually not an expeditious or cost-effective solution to leave it to the project company to acquire easements directly from the owners of the properties concerned. Instead it is more frequent that those easements are acquired by the host Government, through expropriation procedures carried out simultaneously with the expropriation of the project site.

15. A somewhat different alternative might be for the law itself to provide the type of easements given to the project company, without necessarily requiring the expropriation of the property to which such easements pertain. Such an approach might be used in respect of sector-specific legislation, where the host Government deems it possible to determine, in advance, certain minimum easements that might be needed by the project company. For instance, a law specific to the power generation sector may lay down the conditions under which the concessionaire obtains a right of cabling for the purpose of placing and operating basic and distribution networks on property belonging to third parties. Such a right may be needed for a number of measures, such as establishing or placing underground and overhead cables, as well as establishing supporting structures and transforming and switching equipment; maintaining, repairing and removing any of those installations; establishing a safety zone along underground or overhead cables; removing obstacles along the wires or encroaching on the safety zone.

16. Under some legal systems, the project company might be under an obligation to pay compensation to the owner, as would have been due in the case of expropriation, should the nature of the easement be such that the use of the property by its owner is substantially hindered.

3. Exclusivity

17. One of the central issues dealt with in project agreements is whether the right to operate the infrastructure or to provide the service is exclusive or whether competing infrastructure will be allowed to operate. Exclusivity may concern the right to provide a service in a particular geographical region (e.g. a communal water distribution company) or embrace the whole territory of the country (e.g. a national railway company); it may relate to the right to supply one

particular type of goods or services to one particular customer (e.g. a power generator being the exclusive regional supplier to a power transmitter and distributor), or to a limited group of customers (e.g. a national long-distance telephone carrier providing connections to local telephone companies).

18. For countries wishing to adopt general enabling legislation on privately financed infrastructure projects, a flexible approach to deal with the issue of exclusivity may be for the law to provide that the Government is authorized to grant exclusive concessions when it is deemed to be in the public interest, such as in cases where the exclusivity is justified for reasons of technical or economical viability. The awarding authority may be required to state the reasons for granting an exclusive concession for each particular case. Such general legislation may be supplemented by sector-specific laws regulating the issue of exclusivity in a manner suitable for each particular sector (see chapter II, "Sector structure and regulation", ___).

19. An additional issue that may be raised in some projects is whether the project company may be given an assurance that no competing infrastructure will be allowed to operate. Some national laws contain provisions whereby the Government undertakes not to facilitate or support the execution of a parallel project that might generate competition to the project company. In some cases, the law contains an undertaking by the Government that it will not alter the terms of such exclusivity to the detriment of the project company without the project company's consent. In other countries, such an undertaking may be implied in general rules applying to concessions or in general principles of administrative law particularly where the relevant activity is or used to be the object of a State monopoly.

20. Provisions of this type may be intended to foster the confidence of project company shareholders and lenders that no parallel competing project will be carried out or that the basic assumptions under which the project was awarded will be respected. However, they may limit the ability of the host Government to deal with changed circumstances as the public interest may require. For instance, the required tariff level to allow profitable exploitation of a toll road may exceed the paying capacity of low-income segments of the public. Thus, the host Government may have an interest in maintaining open to the public a non-toll charging road as an alternative to a new toll road. These arrangements are not unusual for road transportation projects.

21. Therefore, it may be preferable for the law to authorize the host Government and the project company to find a suitable solution in the project agreement, rather than regulating the matter in the same fashion for all projects. The possibility of subsequent changes in the host Government's policy for the sector concerned, including a decision to promote competition or to build parallel infrastructure, could further be dealt with by the parties in the provisions dealing with changes of circumstances (see chapter VIII, "Delays, defects and other failures to perform", ___).

4. Legal status of the concessionaire

22. Project agreements typically contain provisions on the legal status of the concessionaire and deal with the question whether the concessionaire has to be established as an independent legal entity or whether the project may be awarded collectively to a project consortium. Provisions on these matters are often contained in national legislation on privately financed infrastructure projects as well.

23. As understood in business practice, a consortium is a contractual arrangement whereby a group of enterprises undertakes to cooperate in carrying out a project without integrating into an independent legal entity. Consortia have been widely used in the construction industry for the development of large, capital-intensive projects requiring technical expertise in different fields. Consortia are commonly regarded as purely contractual arrangements which do not have a juridical personality of their own. However, there is no uniform legal regime governing consortia. They may fall under different contractual categories provided in national laws and the legal status of consortia as well as the rights and obligations of their members vary in different legal systems.

24. Forming a project consortium may present some advantages, such as more flexibility in dealings among the consortium members and with their business partners than in a separate project company. Avoiding double taxation may also be a reason for choosing not to establish an independent legal entity in the host country, in case there is no bilateral double taxation agreement between the host country and the country or countries where the foreign investors have their residence for taxation purposes. There might also be instances where the host Government would wish to retain the possibility of engaging consortia for infrastructure projects, depending on the scale and nature of the project, or with a view to holding all consortium members jointly liable for the entire project.

25. For those countries that wish to retain such possibility, the law might give the awarding authority the option to award the project to a consortium or to require that a separate legal entity be established by the selected project consortium, depending on the needs of the project. However, a number of issues would need to be addressed in the project agreement, and extensive negotiations and detailed provisions might be required to ensure coordination among members of the consortium, adequate liaison with the host Government, as well as clarifying the extent of responsibilities and liabilities of each of the members of the consortium for the execution of the project.1/

1/ A brief discussion of issues arising out of contracting construction works with a non-integrated group of enterprises is contained in the *UNCITRAL Construction Legal Guide* (chapter II, "Choice of Contracting Approach", paras. 9-16). Some of the issues mentioned therein might also apply, *mutatis mutandis*, to negotiations concerning privately financed infrastructure projects, including the following: how the difficulty of bringing a claim against consortium members from different countries, should a dispute arise, may be

26. More common, however, are legislative provisions requiring that the concessionaire be established as an independent legal entity. From the perspective of the host Government, an independent legal entity facilitates coordination in the execution of the project and may provide a mechanism for protecting the interests of the project, which may not necessarily coincide with the individual interests of all of the consortium members. This aspect may be of particular importance where significant portions of the services or supplies required by the project are to be provided by members of the project consortium. Since a substantial part of the liabilities and obligations of the project company, including long-term ones (project agreement, loan and security agreements, construction contracts), are usually agreed upon at an early stage, the project may benefit from being independently represented at the time those instruments are negotiated.

27. The host Government may further wish to require that the project company be established under the laws of the country. The host Government may consider that the exercise of its regulatory and monitoring functions in respect of the services provided by the project company might be hindered if the project company were subject to the laws of a foreign jurisdiction. Furthermore, given the public interest in the project company's activities, the host Government may wish that the project company comply with national accounting and publicity provisions (e.g. publication of financial statements; publicity requirements concerning certain corporate acts). However, such a requirement emphasizes the need for the host Government to have adequate company laws in place (see chapter I, "General legislative considerations", paras. 46-49). The ease with which the project company can be established, with due regard to reasonable requirements deemed to be of public interest, may help to avoid unnecessary delay in the implementation of the project.

28. The appropriate time for the establishment of the project company is a matter to be considered in the light of the different interests involved in a typical project. Moved by the interest to start the implementation phase as soon as possible, some host Governments might be inclined to require that the project company be established at the earliest possible stage. However, it should be borne in mind that firm and final commitments by the lenders and other capital providers typically may not be available prior to the final award of the concession, particularly where a separate legal entity is the envisaged vehicle for raising funds for the project, such as in a "project finance" transaction (see "Introduction and background information on privately financed infrastructure projects", paras. 68-71). Therefore, it is generally advisable to

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overcome; how the dispute-settlement clause may be formulated so as to enable any dispute between the host Government and several or all the members of the consortium to be settled in the same arbitral or judicial proceeding; how guarantees to be given by third parties as security for performance and quality guarantees to be given by members of the consortium are to be structured; what ancillary agreements may have to be entered into by the Government; whether there are any mandatory rules of the law governing an agreement with a group of contractors.

require that the project company be established within a reasonably short period after, but not before, the award of the project.

29. Another important issue in connection with the establishment of the project company concerns the equity investment required for the establishment of the project company. The host Government has a legitimate interest in seeking an equity level that ensures a sound financial basis for the project company and guarantees its capability to meet its obligations. Such interest may be satisfied by requiring that the project company be established with a certain minimum capital. In some countries, that issue is dealt with in the law itself, by prescribing a fixed sum or establishing a percentage of the total project cost as the minimum capital of the project company. In other countries, these issues are not addressed in the legislation and are left for the procuring entity to decide, sometimes after negotiations with the selected project consortium.

30. The total investment needed as well as the ideal proportion of debt and equity capital vary from project to project so that it would normally be difficult to establish a fixed sum or percentage that would be adequate for all instances. Thus, it may be undesirable to provide a legislative requirement of a fixed sum as minimum capital for all companies carrying out infrastructure projects in the country. A more flexible approach might be to establish individual requirements taking into account the particular circumstances of each project or type of infrastructure. Where the total expected cost of the project cannot be estimated in advance by the awarding authority, the minimum capital required for the establishment of the project company could be indicated in the solicitation of tenders or request for proposals. Where it is not feasible to estimate in advance the project cost, or in the event the host Government prefers to negotiate the amount or ratio of equity investment offered by the selected project consortium, the awarding authority might prefer to have the flexibility to arrive at an adequate minimum capital in the course of the selection process. In countries where the project is awarded by a formal act of the host Government, such as a decree or notice of award, the required minimum capital of the project company could be indicated in such act.

31. In addition to the question of minimum capital, national laws may contain provisions concerning the form under which the project company has to be organized. Some laws specifically require that the project company be incorporated as a certain type of company, while other laws make no provision on this subject. In cases where it is considered important to specify the form in which the project company is to be established, it is desirable to bear in mind the interest of the consortium members in ensuring that their liability will be limited to the amount of their investment. In order to avoid a subsidiary liability for payment of the project company's debts, its shareholders will normally prefer a corporate form in which their liability is limited to the value of their shares in the company's capital, such as a joint stock company. They would be unwilling to carry out a project that would require them to assume unlimited liability for the project company's debts.

32. Some laws contain provisions concerning the scope of activities of the project company, requiring, for instance, that they be limited to the development and operation of a particular project. Such restrictions might serve the purpose of ensuring the transparency of the project's

accounts and preserving the integrity of its assets, by segregating the assets, proceeds and liabilities of this project from those of other projects or other activities not related to the project. Also, such a requirement may facilitate the assessment of the performance of each project since deficits or profits could not be covered with, or set off against, debts or proceeds from other projects or activities. At the same time, however, the host Government might be interested in reserving the possibility of integrating other projects under a common management, in the event the same project company is awarded a complementary project in a separate selection process.

33. The host Government might also be interested in ensuring that the statutes and by-laws of the project company will adequately reflect the obligations assumed by the company in the project agreement, and that no decision will be made that might hinder the execution of the project. Therefore, the law may provide that changes in the statutes and by-laws of the project company require prior authorization by the host Government. In other countries such a level of control is achieved by requiring the participation of the host Government, as a privileged shareholder, in the project company, with the proviso that certain decisions necessitate the positive vote of the host Government in the shareholders' or board's meeting. In requiring governmental approval for modifications of the statutes and by-laws of the project company or for other corporate decisions, it is desirable to weigh the public interests represented through the State against the need for affording the project company the necessary flexibility for the conduct of its business. The daily management of the project would be impaired if even minor matters concerning the company's internal affairs routinely required prior governmental clearance. One possible solution might be to limit the right of the host Government to object to a proposed amendment to those cases that concern provisions deemed to be of essential importance (e.g. amount of capital, classes of shares and their privileges, liquidation procedures) and which could be identified in the project agreement.

34. The host Government may have a legitimate interest in ensuring that the original members of the project consortium maintain their commitment to the project throughout its duration and that they will not be replaced by entities unknown to the host Government. Thus, the law may provide, in addition to the matters mentioned above, that the transfer of effective control over the project company requires the prior approval of the host Government.

5. Assignment of the concession

35. Concessions are granted in view of the particular qualifications and reliability of the concessionaire and in most legal systems they are not freely transferable. Therefore, national laws frequently prohibit the assignment of the concession without the consent of the Government, which may also be required for a transfer of the right to control the project company. General legislative provisions of this type may promote the confidence of the public in the control being exercised by the Government in respect of the qualifications of infrastructure operators or public service providers.

36. Some countries have found it further useful to mention in the legislation the conditions under which an approval to the transfer of a concession prior to its expiry may be granted, such

as, for example, acceptance by the new concessionaire of all obligations under the project agreement and evidence of the new concessionaire's technical and financial capability as necessary for providing the service. General legislative provisions of this type may be supplemented by specific provisions in the project agreement setting forth the scope of those restrictions, as well as the conditions under which the consent of the host Government may be granted.

37. Unlike a full assignment, a subconcession involves the transfer, to another entity, of the responsibility to carry out one particular activity falling under the concession. In cases where the project company is given the right to provide ancillary services, or where the concession involves multiple activities capable of being carried out separately, the project company may wish to engage another entity to carry out some of those activities by way of a subconcession. Where the concession itself is not transferable, there may be obstacles to a subconcession without legislative authorization. Under normal circumstances, however, the host Government would have no compelling reason for excluding altogether the possibility of subconcessions, provided that it can be satisfied of the reliability and the qualifications of the subconcessionaire. It may therefore be desirable for the law to clarify that the concessionaire is authorized to award subconcessions, subject to prior approval by the host Government.

38. Another related issue concerns the method for selecting a subconcessionaire. Some countries have special rules governing the award of contracts by public service providers, and in some countries the law expressly requires the use of tendering proceedings for the award of subconcessions. Rules of this type were often adopted at times where nearly all infrastructure was owned and operated by the State, with little or marginal private sector investment. Their purpose was to ensure economy, efficiency, integrity and transparency in the use of public funds. However, in the case of infrastructure projects implemented by privately-owned entities, there may no longer be a compelling reason or public interest for prescribing to the concessionaire the procedure to be followed for the award of subconcessions.

6. Security interests

39. The financing documents for privately financed infrastructure projects typically include extensive security arrangements. Even in cases where the potential market value of the infrastructure might be less than the cost of the investment, security in form of tangible assets might cover at least part of the sums borrowed by the project company. Security over negotiable instruments, receivables and intangible rights might also be important factors for reducing the lenders' exposure to the project risks and possibly enhancing the terms of the loans. Thus, the project company will normally have an interest in being able to pledge to the lenders all or some of the assets, property and rights that arise out of the concession.

(a) Security over the physical assets

40. Legal obstacles to the creation of security interests over the physical assets comprised in the infrastructure may arise where those assets remain in the property of the State throughout the

project term. If the project company lacks the title to the property it will in many legal systems have no (or only limited) power to encumber such property.

41. However, in some countries the creation of some form of security may be possible, particularly where the project company is granted a leasehold interest or right to use the relevant property. Such security would not attach to the property itself, but to the rights and interests granted to the project company under the project agreement. Furthermore, security interests may also be created where the concession encompasses different types of State property, such as when title to adjacent land (and not only the right to use it) is granted to a railway company in addition to the right to use the public infrastructure.

42. It is advisable that the law expressly clarify the extent to which the project company may create security interests over the physical assets comprised in the infrastructure, for instance by indicating the types of assets in respect of which such security interests may be created or the type of security interests that is permissible. However, the Government will be interested in that security interests created by the project company do not adversely affect the project. Therefore, the law may require the approval of the Government, usually to be reflected in the project agreement, in order for the project company to create such security interests.

(b) Security over intangible assets

43. The right to operate the infrastructure is in most cases not transferable without the consent of the Government, a circumstance which usually precludes the creation of security interests over the concession or licence. However, even if the concession itself may not be pledged, the law in some countries authorizes the project company to create security interests over the rights arising out of the concession or licence or the proceeds therefrom. Those proceeds typically include the tariffs charged to the public for the use of the infrastructure or the price paid by the customers for the goods or services provided by the concessionaire. They may also include the revenue of ancillary concessions. Security of this type is a typical element of the financing arrangements negotiated with the lenders.

44. Security interests in the form of assignments or pledges of the proceeds of the concession do not affect the Government's title to the physical assets of the concession and usually do not raise the same policy concerns that might be raised by mortgages or similar charges. However, since the enforcement of some of such security might lead to situations where creditors substitute for the concessionaire in the exercise of certain rights arising out of the concession agreement, such security interests may affect the Government, the public or the project company's contracting parties or customers. Therefore, it may be useful for the law to provide that, for the purpose of financing the construction or operation of the facility, the project company may, with the consent of the Government, create any form of security over the rights arising from the project agreement, provided that the enforcement of such security does not affect the obligations of the project company under the agreement with regard to the project or its operation.

(c) Security over shares of the project company

45. The establishment of security interests over the shares of the project company raises, in principle, concerns similar to those raised by an assignment of the concession. Where the concession may not be assigned or transferred without the consent of the host Government, the law sometimes prohibits the establishment of liens or other security over the shares of the project company. It should be noted, however, that security over the shares of the project company is a type of security commonly required by lenders in project finance transactions and that general prohibitions on the establishment of such security may unnecessarily limit the project company's ability to raise funding for the project. As with other forms of security, it might therefore be useful for the law to authorize the project company to create such security subject to the host Government's prior approval.

7. Duration

46. The desirable duration of a project agreement may depend on a number of factors, such as the operational life of the facility or the time needed for the project company to repay its debts and amortize the initial investment. Therefore, it might not be feasible for the law to establish a duration period that would be appropriate to all types of projects. However, a number of countries have found it desirable to adopt legislative provisions limiting the duration of infrastructure concessions to a maximum number of years. Some laws provide for a combined system requiring that the project agreement should provide for the expiry of the concession once the debts of the project company have been fully repaid and a certain revenue, production or usage level has been achieved, subject to a maximum limit of a fixed number of years. Where it is found desirable to adopt legislative provisions limiting the duration of concessions to a maximum number of years, the limitation should permit fixing a period sufficiently long to allow the project company to fully repay its debts and to achieve a reasonable profit.

47. With regard to the method for calculating the duration of the concession period, national laws offer different solutions. Some laws expressly include the construction phase, as well as any extension given for reasons of force majeure, as part of the concession period. Other laws, however, expressly provide that the time necessary for the execution of the project is not taken into account when calculating the duration of the concession period. Some laws achieve the same result by providing that the period of concession begins to run upon completion of the construction. The rationale for including the construction period in the total concession period is to encourage the project company to complete the construction works ahead of schedule, so as to benefit from a longer period of exploration of the facility. This element of encouragement is not available in case the law excludes the construction from the overall concession period.

C. Specific terms

48. In addition to the essential provisions discussed in the preceding section, project agreements typically deal with a wide variety of other issues which are discussed in the following

chapters of the Guide, such as the extent of Government support provided to the project (see below chapter V, "Government support"); schedule of works (see chapter VI, "Construction phase"); conditions of operation of the infrastructure, level and quality of services, tariff structure and price adjustment provisions (see chapter VII, "Operational phase"); provisions and remedies in the event of default or breach of the project agreement, provisions dealing with changes of circumstances and unforeseen events, performance guarantees and insurance obligations of the project company (see chapter VIII, "Delays, defects and other failures to perform"); transfer of the facility at the end of the project period, possibility of extension and causes of early termination of the project agreement (see chapter IX, "Duration extension and early termination of the project agreement"); provisions on applicable law and dispute resolution mechanisms (see chapter X, "Governing law" and chapter XI, "Settlement of disputes").

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